



# R-CALF USA

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June 16, 2006

### PUBLIC DOCUMENT

Ms. Marilyn Abbott  
Secretary  
United States International Trade Commission  
500 E Street, S.W.  
Washington, D.C. 20436

Re: R-CALF USA Prehearing Brief Regarding the Fifth Update of The  
Economic Effects of Significant U.S. Import Restraints (Inv. No. 332-  
325)

Dear Ms. Abbott:

The Ranchers-Cattlemen Action Legal Fund – United Stockgrowers of America (R-CALF USA) appreciates this opportunity to submit its views regarding the Commission's investigation on *The Economic Effects of Significant U.S. Import Restraints*. R-CALF USA is a non-profit association that represents over 18,000 U.S. cattle producers in 47 states across the nation. R-CALF USA's mission is to represent the U.S. cattle industry in trade and marketing issues to ensure the continued profitability and viability of independent U.S. cattle producers. R-CALF USA's membership consists primarily of cow-calf operators, cattle backgrounders, and feedlot owners. Various main street businesses are associate members of R-CALF USA.

In developing the fifth update of its investigation into the economic effects of U.S. import restraints, the Commission is charged with assessing the impact of U.S. import restraints on U.S. consumers and firms, on the income and employment of U.S. workers, and on the net economic welfare of the United States. In previous investigations, the Commission has regularly assessed the impact of liberalizing U.S. restraints on imports of fresh, chilled, or frozen beef.<sup>1</sup>

<sup>1</sup> See *The Economic Effects of Significant U.S. Import Restraints, Fourth Update 2004*, Inv. No. 332-325, USITC Pub. No. 3701 at 51 – 58 (June 2004). The beef products examined in the report, and in this testimony, include fresh, chilled, or frozen beef found at HTS subheadings 0201 and 0202.

R-CALF USA believes there are a number of important factors that have not received extensive analysis in previous investigations that the Commission should consider in this fifth update. In particular, R-CALF USA urges the Commission to weigh the following in assessing the economic effects of liberalizing U.S. import restraints on beef:

- The adequacy of traditional economic modeling in predicting the likely effect of liberalization in beef trade, particularly the impact on upstream cattle producers;
- External barriers to U.S. exports that have resulted in a large U.S. trade deficit in fresh, chilled and frozen beef since 2003;
- The demonstrated ability of certain large producers to export to the U.S. in excess of quota levels despite out-of-quota tariffs; and
- The cumulative impact of bilateral and regional Free Trade Agreements that liberalize trade in beef.

#### **I. Economic Modeling and the Impact of Beef Trade Liberalization**

In the fourth update of the *Economic Effects* investigation, the Commission employed a general equilibrium model to estimate economywide and sectoral effects of significant import restraints.<sup>2</sup> The Commission declined to apply a partial equilibrium model to examine the sectoral impacts of import restraints, though the original request for the *Economic Effects* investigation from the U.S. Trade Representative asked that partial equilibrium frameworks be used in the analysis of liberalization in individual sectors.<sup>3</sup> While employing a general equilibrium model for both sectoral and economywide analyses allows for comparisons between the two types of analyses, it may also limit the reliability of economic impact estimates at the sectoral level. A partial equilibrium model allows the Commission to take into account decreasing returns to scale, and it allows the Commission to identify the likely direct effects of a discrete policy change on a narrow product category. Application of a general equilibrium model to sectoral analyses, by contrast, assumes no declining returns and assumes that full equilibrium has been reached throughout the economy as factors adjust to their most productive uses. In sectors that are import-sensitive, such as cattle and beef, it is particularly appropriate to employ a partial equilibrium model as originally requested by USTR.

In addition, the Commission should devote particular attention to how liberalizing U.S. import restrictions on beef will impact upstream U.S. cattle producers. In previous updates, the Commission has sometimes included a discrete analysis of impacts on upstream producers and sometimes not. In its first update to the investigation in 1995, for example, the Commission found that the sector most dramatically impacted by meat trade liberalization would be the live animal sector.<sup>4</sup> The Commission estimated output

<sup>2</sup> *Id.* at 2.

<sup>3</sup> *Id.* at Appendix A.

<sup>4</sup> See *The Economic Effects of Significant U.S. Import Restraints, First Biannual Update*, Inv. No. 332-325, USITC Pub. No. 2935 at 4-11 – 4-14 (December 1995).

losses for the sector of \$273 million.<sup>5</sup> In the last update, however, the Commission did not provide any detailed analysis of the impact of beef import liberalization on upstream cattle producers.<sup>6</sup>

In this update, the Commission should expand on its earlier practice and analyze the impact of beef import liberalization on cattle producers. The Commission has previously found that the most significant impact of beef import liberalization is likely to be the impact on cattle producers. In fact, in its evaluation of the economic effects of increased beef access for Australia under the U.S. – Australia FTA, the Commission noted that an analysis from the perspective of cattle producers is likely to be more useful and relevant than an analysis of trade impacts from the perspective of the meat packing industry:

... U.S. beef packers operate on the margin between wholesale beef prices and slaughter cattle prices. Furthermore, market structure suggests that processors can eventually pass most, if not all, of any decrease in the price of wholesale beef that results from increased import access ... on to U.S. cattle producers in terms of lower slaughter cattle prices. Therefore, this section addresses the impact of the FTA on the domestic industry from the focus of live cattle producers rather than beef processors.<sup>7</sup>

In its study of the Australia FTA, the Commission also noted the high sensitivity of cattle prices to increases in beef supply. The Commission stated that each percentage point of increase in beef supply was likely to translate into a decrease in live cattle prices of 2 percent.<sup>8</sup> The Commission should expand upon this analysis in the current investigation.

In particular, the Commission should consider how to account for the particular structure of the domestic cattle and beef market in its analysis. The GAO has recommended that the Commission take market structure factors into account in its economic analyses of cattle trade, finding that neither the CGE model nor other economic models used by the ITC “explicitly account{ } for concentration, marketing agreements, and forward contracts.”<sup>9</sup> These factors are important, because they determine how direct impacts of imports on the meat packing industry will be passed on to downstream consumers and upstream producers.

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<sup>5</sup> *Id.* at 4-12.

<sup>6</sup> See *The Economic Effects of Significant U.S. Import Restraints, Fourth Update 2004*, Inv. No. 332-325, USITC Pub. No. 3701 at 51 – 58 (June 2004).

<sup>7</sup> *U.S. – Australia Free Trade Agreement: Potential Economywide and Selected Sectoral Effects*, Inv. No. TA-2104-11, USITC Pub. No. 3697 at 41, fn. 1 (May 2004).

<sup>8</sup> *Id.* at 44.

<sup>9</sup> U.S. General Accounting Office (now the Government Accountability Office), *Economic Models of Cattle Prices: How USDA Can Act to Improve Models to Explain Cattle Prices*, GAO-02-246 at 8 (March 2002).

The increased leverage of the meat packing industry over cattle prices that results from growing market concentration and new contracting practices will determine how liberalization of beef imports affects cattle prices and thus cattle producers. As former U.S. International Trade Commission Chairwoman Lynn Bragg observed in the Commission's investigation on cattle imports from Canada, "The concentration of packers increases the packers' leverage relative to cattle producers, thus providing packers the ability to use imports [of cattle] to reduce domestic live cattle prices and/or prevent price increases."<sup>10</sup> This insight is equally relevant with regard to imports of beef.

In addition, the structure of the meat packing industry will affect whether and to what extent lowered prices resulting from increased beef imports are fully passed on to beef consumers. Market concentration and contracting practices in the meat packing industry can prevent lower cattle prices from automatically translating into lower beef prices for consumers. This disconnect between the dollar returns to producers and the prices paid by consumers is reflected in the producer's declining share of each retail dollar spent on beef. The Commission should take this dynamic into account in its analysis in order to generate more reliable results.

Concentration among meatpackers has more than tripled since the late 1970s, and today just four beef packing companies control more than 83 percent of the industry.<sup>11</sup> This level of concentration far exceeds other industries, and the rate of growth in concentration is unmatched among other industries for which the Census Bureau collects such data.<sup>12</sup> Such a high level of concentration is indicative of a severe lack of competitiveness in the industry, given that most economists believe competitive conditions begin to deteriorate once the four-firm concentration level exceeds 40 percent.<sup>13</sup>

At the same time that the meatpacking industry has been consolidating dramatically, packers have increasingly used non-traditional contracting and marketing methods that further erode the selling power of cattle producers. Such methods include purchasing cattle more than 14 days before slaughter (packer-fed cattle), forward contracts, and exclusive marketing and purchasing agreements. Together, the four largest packing companies employed such forms of "captive supply" contracting methods

<sup>10</sup> *Live Cattle from Canada*, Inv. No. 731-TA-812 (Final), USITC Pub. 3255 at 50 (November 1999).

<sup>11</sup> J. McDonald et al., *Consolidation in U.S. Meatpacking*, Food and Rural Economics Division, Economic Research Service, U.S. Department of Agriculture, Agricultural Economic Report No. 785 at 7 (February 2000) (hereinafter McDonald) and M. Hendrickson and W. Heffernan, *Concentration of Agricultural Markets*, University of Missouri Department of Rural Sociology, February 2005, available on-line at <http://www.foodcircles.missouri.edu/CRJanuary05.pdf>.

<sup>12</sup> McDonald at 7.

<sup>13</sup> *Economic Concentration and Structural Change in the Food and Agriculture Sector: Trends, Consequences and Policy Options*, Report Prepared by the Democratic Staff of the Committee on Agriculture, Nutrition, and Forestry, United States Senate at 4 – 5 (October 2004).

for a full 44.4 percent of all cattle they slaughtered in 2002.<sup>14</sup> And use of these captive supply methods has been increasing rapidly, rising 37 percent from 1999 to 2002.<sup>15</sup>

Captive supply practices push risks of price instability on to cattle producers and hold down cattle prices.<sup>16</sup> As prices for cattle are artificially depressed and become more volatile, it is cattle producers who pay the price, even when broader demand and supply trends should be increasing returns to producers. The impact of packer concentration and contracting practices is evident in the declining share of each beef retail dollar that actually reaches cattle ranchers. The rancher's share of each retail dollar earned on beef was 47 cents in 2005, down from 56 cents in 1993.<sup>17</sup>

Finally, the Commission should also consider the perishable nature of live cattle in its economic effects analysis. Perishable domestic products such as cattle are likely to experience greater price effects from small increases in imports than non-perishable products, which can be stored and marketed over time to mitigate price competition from limited surges in imports. This option is not available for perishable products such as live cattle, which must be marketed in a very limited window of time. Live cattle producers are thus more susceptible to price volatility due to imports than other kinds of producers, further eroding their selling power in relation to meat packers.

Cattle producers are the sector most likely to experience income, output and employment losses due to liberalization of U.S. beef imports. The Commission should employ a partial equilibrium model, explicitly evaluate the likely impact of beef trade liberalization on upstream cattle producers, and take into account the market concentration and contracting practices in the meat packing industry, as well as the perishable nature of live cattle, in making its assessment.

## II. External Trade Barriers and the U.S. Trade Deficit in Beef

Since the publication of the fourth update of the *Economic Effects* study, U.S. beef exports have declined dramatically due to the closure of export markets after the discovery of a Canadian animal with bovine spongiform encephalopathy (BSE) in Washington state in late 2003. The U.S. exported more than \$3 billion in fresh, chilled or frozen beef in 2003, which fell to \$0.5 billion in 2004 and \$0.8 billion in 2005. Meanwhile, U.S. imports of fresh, chilled or frozen beef have risen since 2003. The U.S.

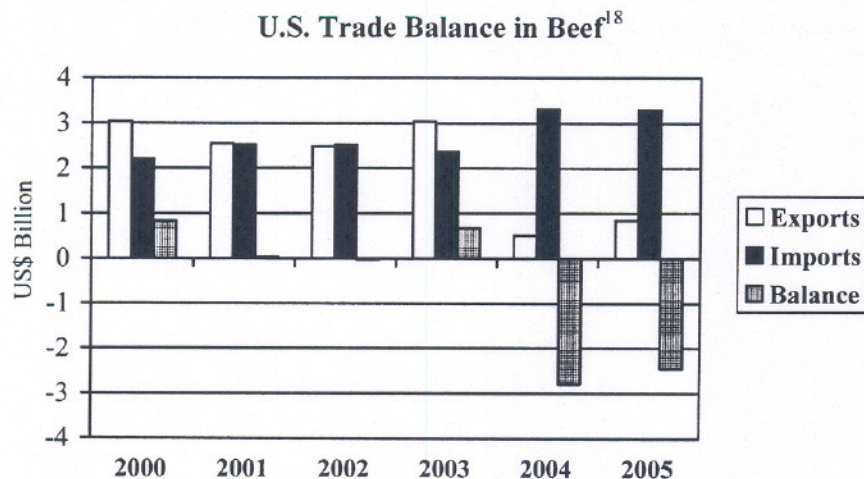
<sup>14</sup> RTI International, *Spot and Alternative Marketing Arrangements in the Livestock and Meat Industries: Interim Report*, Report Prepared for the Grain Inspection, Packers, and Stockyard Administration, U.S. Department of Agriculture at 3-15 (July 2005).

<sup>15</sup> *Id.* at 3-17.

<sup>16</sup> *Id.* at 3-18 – 3-22 and John M. Connor, “The Changing Structure of Global Food markets: Dimensions, Effects, and Policy Implications,” Paper Presented to The Conference on Changing Dimensions of the Food Economy: Exploring the Policy Issues, The Hague, Netherlands at 8 (February 2003).

<sup>17</sup> USDA Economic Research Service, “Beef Values and Price Spreads,” available on-line at <http://www.ers.usda.gov/briefing/foodpricespreads/meatpricespreads/>.

imported \$2.4 billion of fresh, chilled or frozen beef in 2003 and \$3.3 billion in 2005. The result of declining exports and rising imports has been a significant trade deficit in fresh, chilled or frozen beef. The deficit totaled \$2.8 billion in 2004 and \$2.5 billion in 2005.



Closure of foreign markets is preventing a rebound in the domestic cattle sector at a time when such a resurgence would otherwise be expected, with growing domestic beef demand, the closure of the border to imports of cattle from Canada for much of the 2003 to 2005 period, and rising prices for cattle. Instead of the normal rebound in the cattle cycle, the loss of export markets is thwarting a full recovery in the domestic cattle and beef sector. Restraints in external markets are artificially reducing the size of the U.S. cattle industry, as imports are increasing and seizing a large share of domestic consumption.

- In 2003, all cattle and calf marketings totaled 56.8 billion pounds.<sup>19</sup> In 2004, the volume marketed fell to 53.8 billion pounds, and in 2005 it fell again to 53.1 billion pounds.<sup>20</sup>
- The number of cattle operations in the U.S. dropped from 1,013,570 in 2003 to 982,510 in 2005, and the cattle and calf inventory fell from 96 million head to 95 million from 2003 to 2005.<sup>21</sup>
- Overall U.S. beef production (domestic and export combined) declined 6 percent from 2003 to 2005 (by quantity).<sup>22</sup>

<sup>18</sup> U.S. Department of Commerce, Census Bureau, Foreign Trade Statistics. Data for HTS 0201 and 0202.

<sup>19</sup> USDA, *Meat Animals Production, Disposition, and Income 2003 Summary* at 1 (April 2004).

<sup>20</sup> USDA, *Meat Animals Production, Disposition, and Income 2004 Summary* at 1 (April 2005) and USDA, *Meat Animals Production, Disposition, and Income 2005 Summary* at 1 (April 2006).

<sup>21</sup> U.S. Department of Agriculture, National Agricultural Statistics Service, Agricultural Statistics Database, *U.S. and All States Data – Cattle and Calves*.

<sup>22</sup> U.S. Department of Agriculture, Production, Supply and Distribution Database, *Meat, Beef and Veal*, available on-line at <http://www.fas.usda.gov/psd/> (hereinafter "USDA PSD Database").

- From 2003 to 2005, production employment in the animal (except poultry) slaughter industry fell from 134,900 to 128,800 and production employment in meat processing fell from 96,900 to 93,800.<sup>23</sup>
- U.S. beef imports increased both in absolute terms and as a portion of domestic consumption from 2003 to 2005. Beef imports accounted for a higher portion of domestic U.S. consumption in 2005 (12.9%) than they did in 2003 (11.1%).<sup>24</sup>

While U.S. product has been all but eliminated from foreign export markets, including such key markets as Japan and Korea, other beef-exporting countries have stepped into those markets to supply a portion of the demand no longer served by the U.S. Yet, at the same time, these beef-exporting countries have continued to export to the U.S. in steady and even increasing amounts. Thus, even as markets re-open to U.S. beef exports, the U.S. is likely to continue to face not only significant volumes of beef imports at home, but also a larger presence of competing foreign beef production abroad. In addition, as long as other countries maintain TRQs on beef imports that are more restrictive than U.S. import restraints, the U.S. will continue to face barriers in external markets and be a highly attractive market for global exporters.

### III. Impact of U.S. Import Restrictions on Exporters

Another new development since the last update of the *Economic Effects* investigation that merits the Commission's consideration is the fact that large beef producing nations have recently demonstrated the ability to export large quantities to the U.S. regardless of TRQ levels. While import TRQs can prove to be a cap on imports from some countries, that does not appear to be the case for all countries.

For example, Uruguay has emerged as the fourth largest exporter of fresh, chilled or frozen beef to the U.S. just two years after re-gaining access to the U.S. market. Uruguay was declared FMD-free in May of 2003,<sup>25</sup> and it rapidly became a major exporter of beef to the U.S. Uruguay exported 26,180 MT of beef to the U.S. in 2003.<sup>26</sup> By 2004, in just one year, Uruguay's exports to the U.S. nearly quintupled to 128,189 MT. Exports rose again in 2005, to 173,392 MT. Overall, U.S. imports from Uruguay increased by 5,623 percent from 2003 to 2005.

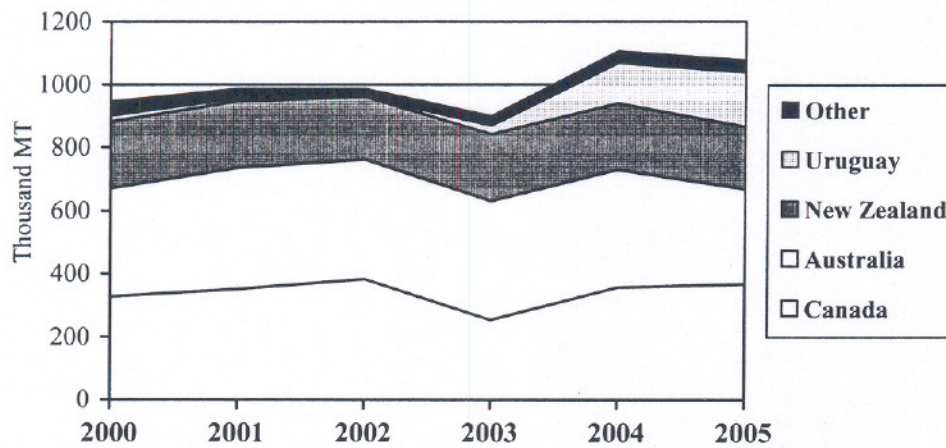
<sup>23</sup> U.S. Department of Labor, Bureau of Labor Statistics, Current Employment Statistics, Animal (except poultry) Slaughter and Meat Processing, Production Workers, NAICS 311611, 311612 and 311613. While these numbers include other animal products such as pork and lamb, the decline in employment since 2003 contrasts markedly with steady or growing employment in these sectors over the previous ten years.

<sup>24</sup> USDA PSD Database.

<sup>25</sup> See 68 Fed. Reg. 31940 (May 29, 2003).

<sup>26</sup> U.S. Department of Commerce, Census Bureau, Foreign Trade Statistics. Data for HTS 0201 and 0202.

Major Exporters of Beef to the U.S.<sup>27</sup>



The U.S. TRQ on beef imports from Uruguay appears to have imposed little, if any, significant restraint on these imports. The U.S. has a TRQ of 20,000 MT for imports of fresh, chilled or frozen beef from Uruguay, and the U.S. imposes a tariff of 26.4 percent on imports entering out of quota.<sup>28</sup> Yet Uruguay shipped six times its quota allocation to the U.S. in 2004 and more than eight times that quota amount in 2005. In 2005, Uruguay filled its annual 20,000 MT quota before the end of February.<sup>29</sup> Uruguay continued to ship out of quota for the rest of the year, paying the 26.4 percent tariff on more than 150,000 MT of exports. Though other major exporters, such as Australia and New Zealand, generally stay within their quota amount, Uruguay is willing to swallow the out-of-quota tariff in order to ship large volumes to the U.S. In 2005, even with an import quota that is one-tenth as big as New Zealand's, Uruguay exported almost as much beef to the U.S. as New Zealand did.

The Commission should consider the Uruguay example as it evaluates the impact of U.S. import restraints on beef. While TRQs may be limiting imports from Australia and New Zealand to some extent, they have not proven to be as effective in the case of Uruguay. As more large global producers address their health and safety problems and gain access to the U.S. market, similar patterns may emerge for additional countries. For example, Argentina and Brazil presently ship no fresh, chilled or frozen beef to the U.S. due to FMD.<sup>30</sup> Yet these countries are becoming increasingly productive and increasingly export oriented. Brazil and Argentina were the first and third largest beef

<sup>27</sup> U.S. Department of Commerce, Census Bureau, Foreign Trade Statistics. Data for HTS 0201 and 0202.

<sup>28</sup> See Additional U.S. note #3, Chap. 2, HTS.

<sup>29</sup> Information on Uruguay's quota for beef exports to the U.S. and the out-of-quota tariff is from the U.S. Harmonized Tariff Schedule at Chap. 2, subheadings 0201 and 0202.

<sup>30</sup> See 9 C.F.R. § 327.2.

exporters in the world in 2005, up from rankings as the fifth and seventh largest global exporters in 2000.<sup>31</sup>

#### IV. Beef Trade Liberalization under Free Trade Agreements

The Commission should also consider the cumulative impact of beef trade liberalization under bilateral and regional Free Trade Agreements (FTAs). Since 2002, the U.S. has entered into FTAs with a number of beef-producing nations and regions, including Australia, Central America, and Chile. In addition, the U.S. has recently concluded but not yet implemented FTAs with Colombia and Peru that liberalize beef trade. The table below summarizes provisions of these agreements regarding access to the U.S. market for fresh, chilled or frozen beef.

**FTA Access to the U.S. for Fresh, Chilled or Frozen Beef<sup>32</sup>**

	<b>Australia</b>	<b>Chile</b>	<b>DR-CAFTA</b>	<b>Peru</b>
<b>Pre-FTA U.S. Import TRQ</b>	Dedicated quota of 378,214 MT	Access under "all others" quota of 64,805 MT	Access under "all others" quota of 64,805 MT	Access under the "all others" quota of 64,805 MT
<b>Additional FTA Import TRQ in Year 1</b>	15,000 MT <sup>33</sup>	1,000 MT	22,968 MT (combined)	0
<b>Phase Out of TRQ</b>	18 years	4 years	15 years	15 years
<b>Backloaded Phase Out</b>	Yes	No	No	No

As these FTAs are implemented, access to the U.S. market for beef exports from these countries will increase as quotas grow and out-of-quota tariffs decline. At the end of the agreements' phase-out periods, each FTA partner will enjoy unlimited access to the U.S. market for their beef exports, as Canada and Mexico currently do. The U.S. will also see its access to these countries' markets increase, and tariffs on its exports to these countries will eventually reach zero. The U.S. has also gained access to other markets under FTAs with countries that are not large beef producers but do consume beef imports (e.g., Singapore, Bahrain, Morocco, Oman, and the United Arab Emirates). In addition, the U.S. has just begun negotiating an FTA with Korea, which was the third-largest

<sup>31</sup> USDA PSD Database.

<sup>32</sup> Texts of the FTAs are available on the USTR website at [http://www.ustr.gov/Trade\\_Agreements/Bilateral/Section\\_Index.html](http://www.ustr.gov/Trade_Agreements/Bilateral/Section_Index.html). The agriculture market access annexes of the U.S. – Colombia FTA are not yet public, and thus it is not included in this table.

<sup>33</sup> The additional quota amount for beef imports from Australia does not come into effect until the U.S. resumes global beef exports at their 2003 level or three years expire, whichever is sooner.

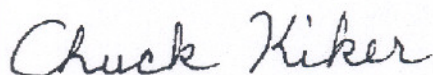
export destination for U.S. beef before Korea closed its market in late 2003. Korea's import ban is still in place as of this writing.

Finally, if the current Doha Round of negotiations at the WTO concludes successfully, there is likely to be further liberalization of beef trade. The Commission may wish to take the likely outcome of these negotiations, as well as the cumulative impact of current and planned FTAs, into account in its economic impact analysis.

#### **V. Conclusion**

R-CALF USA urges the Commission to consider the factors discussed above – economic modeling that adequately accounts for the impact of beef imports on upstream cattle producers, external barriers to U.S. beef exports and the U.S. beef trade deficit, the effectiveness of U.S. TRQs on new sources of imports, and the cumulative impact of existing market-opening agreements – in its analysis of the economic effect of U.S. restraints on beef imports. We appreciate the opportunity to present our views to the Commission in this important matter.

Sincerely,

A handwritten signature in cursive script that reads "Chuck Kiker".

Chuck Kiker  
President, R-CALF USA